

## Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B03

PLR-105441-10

Date:

July 20, 2010

## LEGEND

X =

Trust =

A =

B =

State =

Date =

1

Date =

2

Date =

3

Date =

4

Date =

5

Year =

1

Year =

2

Year =

3  
n =  
Dear :

This letter responds to your letter dated January 27, 2010, and subsequent correspondence, submitted on behalf of X by its authorized representative, requesting a ruling under § 1362(f) of the Internal Revenue Code.

### FACTS

X was incorporated under the laws of State on Date 1. X elected to be an S corporation effective Date 2. On Date 3, A and B transferred shares of X's stock to Trust. Trust was not a trust identified in § 1362(c)(2); therefore, Trust was an ineligible shareholder and X's S corporation election terminated on Date 3.

X represents that there was no intent to terminate X's S corporation election and that the transfer to Trust was inadvertent and not motivated by tax avoidance or retroactive tax planning. After Trust was informed of its status as an ineligible shareholder, the trustee of Trust on Date 4 distributed the stock to A. For all taxable years, X and X's shareholders reported income consistent with X qualifying as an S corporation. In addition, X and X's shareholders agree to make any adjustments consistent with the treatment of X as an S corporation as may be required by the Secretary with respect to the period specified by § 1362(f).

### LAW AND ANALYSIS

Section 1361(a)(1) provides that the term "S corporation" means, with respect to any taxable year, a small business corporation for which an election under § 1362(a) is in effect for such year.

Section 1361(b)(1) defines a "small business corporation" as a domestic corporation which is not an ineligible shareholder and which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate, a trust described in § 1361(c)(2), or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1362(d)(2)(A) provides that an election under § 1362(a) shall be terminated whenever (at any time on or after the 1<sup>st</sup> day of the 1<sup>st</sup> taxable year for which the corporation is an S corporation) such corporation ceases to be a small business corporation.

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation was terminated under § 1362(d)(2) or (3); (2) the Secretary

determines that the circumstances resulting in such termination were inadvertent; (3) no later than a reasonable period of time after discovery of the circumstances resulting in such termination, steps were taken so that the corporation for which the termination occurred is a small business corporation; and (4) the corporation for which the termination occurred, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make the adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to this period, then, notwithstanding the circumstances resulting in the termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

Section 1.1362-4(d) of the Income Tax Regulations provides that the Commissioner may require any adjustments that are appropriate. In general, the adjustments required should be consistent with the treatment of the corporation as an S corporation during the period specified by the Commissioner.

### CONCLUSION

Based solely on the facts submitted and representations made, we conclude that X's S corporation election was terminated on Date 3 when X's stock was contributed to Trust because Trust was an ineligible shareholder. We further conclude that the termination was inadvertent within the meaning of § 1362(f). Pursuant to the provisions of § 1362(f), X will be treated as continuing to be an S corporation on and after Date 3, unless X's S corporation election is otherwise terminated under § 1362(d) and provided that the following conditions are met. From Date 3, A will be treated as directly holding the shares of X held by Trust. A must file within 120 days of this ruling any amended returns for Years 1, 2, and 3 as necessary to treat A as the owner of the X stock held by Trust. As an adjustment under § 1362(f)(4), A must send a payment of \$n and a copy of this letter to the following address: Internal Revenue Service, Cincinnati Service Center, 201 West Rivercenter Blvd., Covington, KY 41011, Stop 31, Terri Lackey, Manual Deposit. This payment must be sent no later than Date 5.

This ruling is contingent upon X and all its shareholders treating X as having been an S corporation for the period beginning on Date 3, and thereafter. The shareholders of X must include in their income their pro rata share of separately stated and nonseparately computed items of X as provided in § 1366, make any adjustments to basis as provided in § 1367, and take into account any distributions made by X as provided in § 1368. This ruling is contingent upon X and each of its shareholders filing any amended returns and making such adjustments that are necessary to properly reflect the reporting of X's items of S corporation income.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this

requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

If all of the above conditions are not met, then this ruling is null and void. Furthermore, if these conditions are not met, X must notify the Cincinnati Service Center that its S corporation election has terminated.

Except for the specific ruling above, no opinion is expressed or implied concerning the federal tax consequences of the facts of this case under any other provision of the Code. Specifically, no opinion is expressed or implied regarding X's eligibility to be an S corporation.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the ruling request, it is subject to verification on examination.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,

/s/

James A. Quinn  
Senior Counsel, Branch 3  
Office of the Associate Chief Counsel  
(Passthroughs & Special Industries)

Enclosures (2)

Copy of this letter

Copy of this letter for § 6110 purposes